

MINUTES

**MONTANA SENATE
57th LEGISLATURE - REGULAR SESSION
FREE CONFERENCE COMMITTEE ON SENATE BILL 512, SENATE BILL 505,
SENATE BILL 506, SENATE BILL 508, HOUSE BILL 600,
and HOUSE BILL 646**

Call to Order: By **CHAIRMAN MACK COLE**, on April 16, 2001 at 3:00 P.M., in Room 317 Capitol.

ROLL CALL

Members Present:

Sen. Mack Cole, Chairman (R)
Rep. Bob Story, Chairman (R)
Sen. Bob DePratu (R)
Rep. Ronald Devlin (R)
Rep. Gary Forrester (D)
Sen. Mike Halligan (D)

Members Excused: None.

Members Absent: None.

Staff Present: Lynette Brown, Committee Secretary
Stephen Maly, Legislative Branch
Jeff Martin, Legislative Branch

Please Note: These are summary minutes. Testimony and discussion are paraphrased and condensed.

Committee Business Summary: **Energy Tax - SB 512, SB 505,
SB 506, SB 508, HB 600, HB 646**

{Tape : 1; Side : A; Approx. Time Counter : 0}

SEN. MACK COLE stated the committee would be dealing with SB 505, SB 506, SB 508, SB 512, HB 600, and HB 646.

SEN. COLE they would begin with SB 512.

Dan Dobbs, Department of Revenue, explained an example of how this tax would work for a hypothetical sale

EXHIBIT (frs85sb0512a01). He said the language in the bill concerning how the tax was worded put everything in net price minus \$45. **Mr. Dobbs** stated the table showed a rate for a net price from \$0 - \$15, with the other rates at \$10 increments. The example worked through calculations in the bill to give rates at different prices. For a price of less than \$45, the tax rate was \$0; for a price of \$45-\$60, you would take the \$0 tax on the 1st \$45, then subtract \$45 from the price with the tax being 20% of the difference. He said by the time a \$70 price was reached, the tax would be \$7. The tax would be \$.60 for each dollar the price was above \$70.

Dan Dobbs provided the committee with **EXHIBIT (frs85sb0512a02)** an example of a sale from a hypothetical generation company selling three million megawatt hours to a distribution company for a fee of \$65 per megawatt hour. He said this would be done for any sale and there would be different sales for different companies at different prices.

SEN. MIKE HALLIGAN asked if the current fiscal note on the bill was accurate. **Dan Dobbs** responded the fiscal note reflected the current bill in its present form. **Mr. Dobbs** added they had some questions about what they may or may not actually be able to tax. The fiscal note was accurate, assuming they were able to tax all of the sales that could be taxed and reflected the latest changes.

SEN. HALLIGAN requested **Mark Richards, Department of Revenue**, to comment on the amendment for this bill which was adopted in committee. **Mr. Richards** explained Section 2, Subsection 5, included energy generated in Montana by fully integrated regulated public utility for the customers within the authorized area. **SEN. HALLIGAN** said he felt that would affect the constitutionality of the bill by treating in-state generators differently. He asked **Mr. Richards** if the department had assessed any of that. **Mr. Richards** replied their recommendation was to remove that from the bill.

SEN. HALLIGAN asked **Mark Richards** if there was a way to draft the information to help their situation out without affecting the constitutionality of the bill. **Mr. Richards** answered he did not know of a way to word that to take care of the problem because it was essentially treating different companies differently. He added the taxes needed to be made as uniform as possible.

SEN. HALLIGAN said he had worked on an amendment that would accomplish what the Department of Revenue to do which he hoped to

be able to distribute to the committee members the following day. He added he wanted to address the issue and the subsection may need to be stricken.

REP. ROBERT STORY asked if the issue was when starting to exempt anybody, the bill would be weakened and susceptible to challenge. **Mark Richards** responded that was true.

REP. STORY asked **Mark Richards** if that needed to be dealt with in exemptions or in transactions; specifically in the rate transactions would be taxed at. **Mr. Richards** replied, currently, the bill did not tax the transaction, but taxed the revenue derived from the transaction, which were two different things. He added the reason the actual transaction should not be taxed was because it may be sold out of state and they did not have nexus over the sale if it was sold out of state. He said Montana could not impose a sales tax on something purchased out of state. **Mr. Richards** said that was why the department was trying to get to the revenue derived which was actually a tax on excess revenue that was measured by the sale of the electrical energy. He stated their recommendation on this bill was to not tax the sale, but try to tax the revenue derived from the sale.

REP. STORY asked **Gene Walborn, Department of Revenue**, to explain how the mechanics of this tax would work; how the revenue of the sale would be determined, especially when it had to be related to megawatt hours. **Mr. Walborn** responded the Department of Revenue would need to create a self-reporting type of tax form. He said the Department would require them to give the Department copies of their sales contracts or documentation proving the price of the sale. **Mr. Walborn** explained the proof of sale would need to be provided, otherwise the Department would need to audit them and verify the sales prices to enable the Department of Revenue to apply the appropriate tax. He said it would work similar to individual income tax or any corporate license tax in the self-employed tax the department would have.

REP. STORY asked **Gene Walborn** how to figure out the situation when dealing with a company that owns both a generation, transmission and distribution all integrated. **Mr. Walborn** answered something would need to be built in defining what an "arms-length transaction" was. He said that situation may not be an arms-length transaction because it was all within the same company. **Mr. Walborn** said MDU was regulated with everything built into the rate structure and would probably not have that kind of profits. If they did make that type of sale, he added, they would need to have to submit that information to the department.

REP. STORY asked **Gene Walborn**, assuming the regulated system had a power cost in the regulated system of over 4 ½ cents, how would it be determined. **Mr. Walborn** replied if they met the criteria of the tax, they would have to remit the information to the department. He said he was yet unsure of how that would work and how they would report the information back to the department.

Mr. Walborn questioned if they had those sales, was it really in excess profits they were receiving that was going to fund the energy for their customers because there would technically not be a sale there. He added if the company had a sale outside of their customer base, then that would fit; however, if it was just to supply electricity to their customers, he was not sure if that was really a sale that occurred.

REP. STORY asked **Gene Walborn** if the definition was adequate to deal with that or would the wording need to be changed to include the arms-length mode included. **Mr. Walborn** responded he would like the wording tuned up in order to answer some of the questions discussed. He said it would be beneficial to change the wording.

REP. STORY asked **Mark Richards** if some of the concerns about exemptions could be solved by changing the definition. **Mr. Richards** said the definition of "arms-length sale" could take care of that problem. He was unsure if a company like MDU fit in this category because they actually delivered bundled electricity to customers as opposed to a generator unit that sold wholesale on the wholesale market. Under this bill, if MDU had some extra electricity and wanted to sell it to California, that would fall under this bill. He was not familiar enough with MDU to know if that would qualify as an actual sale or transaction that took place since it was integrated.

REP. GARY FORRESTER asked **SEN. COLE** how many bills the committee intended to come out with; did the committee intend to come up with one bill that included a form of each of the bills. **SEN. COLE** replied the committee would have to decide as to how they wanted to handle all the bills.

REP. FORRESTER asked **Dan Dobbs** if this bill pertained to PPL. **Mr. Dobbs** answered the Department of Revenue's interpretation was that all the sales made taxable under this bill would be made by PPL.

REP. FORRESTER asked **Dan Dobbs** if they had not looked at the books, one way of putting it, in three or four years; they hadn't been a regulated utility; they bought it fair and square, paid their money, and managed it as they pleased. **REP. FORRESTER** asked **Dan Dobbs** if he knew if \$.045 cents was enough to service

PPL's debt and did he know all the things involved. **Mr. Dobbs** answered the department did not have enough information to answer.

Susan Good, Public Service Commission, answered **REP. FORRESTER**, saying it was correct. She said they had not had an opportunity to determine if the \$.045 was adequate. She added the earlier numbers they had access to were considerably less. **Ms. Good** said they had not seen a lot of changes, other than regular inflation. She was unsure of how they would get access to that information in today's bargaining.

REP. FORRESTER asked **Susan Good** if she could get that information to the committee this week before passage of this bill. She answered she did not think she could get that information this week, but would check with their staff to see if it was possible.

SEN. COLE asked **Jeff Martin, legislative services**, to explain any other items in this bill that needed to be addressed. **Jeff Martin** reiterated the point made by **Mark Richards** to take a careful look at what the exemption sections were, whether needing to revise or eliminating some of the exemptions and to also consider where the revenue was going in the bill. He added, presently, there was a special revenue account set up for a variety of programs administered by the Public Service Commission. **Mr. Martin** stated some other areas would be to look at the termination date to decide if a change needed to be made.

SEN. BOB DEPRATU asked **Jeff Martin** to expand on the difference between money going into the special revenue account as opposed to going into the general fund. **Mr. Martin** answered differences would be: (1) if the money went into the special revenue account for buying down electricity contracts, (2) set up to recruit or retain large employers of 1200 employees and employer and (3) to expand the Universal System Benefit Program. The issue would be of dedicating the revenue to specific types of issues as opposed to the general fund for general purposes.

Stephen Maly, legislative services, added that was a portion of a larger concern and was also imbedded in the exemption portion of the bill. To make this bill effective and legally defeasible to the greatest extent possible, the bill would probably need those kinds of refinements and to make it as clean and clear as possible, he said. He said they had been involved in staff discussions about which exemptions were defensible and which were not and how important it was to segregate the flow of the funds from specific allocations.

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REP. STORY told **Stephen Maly** he understood why there were problems with the exemptions because there would be a problem with the tax if everybody was exempted except one person. **Mr. Maly** added who paid the tax and where the money would go were both a part of a strategy.

REP. STORY asked **Stephen Maly** if there was a legal problem or functional issue by putting into a special revenue account. **Mr. Maly** answered it was a legal issue.

Mark Richards said the problem with the distribution side of the bill was that there was a lot of case law saying you could not raise taxes on people out of state, which included raising taxes and subsidizing your own citizens or your own interests. He said even though an excess profits tax was difficult to pass on to out-of-state consumers, the fact that the distribution included would be a "red light" that maybe the state was trying to pass on the cost to out-of-state consumers. **Mr. Richards** said the bill, as written, even with the distribution, was probably still defeasible; however, it would be easier if the distribution part were not included.

SEN. HALLIGAN asked **Mark Richards** if the money went back to the company that paid it through the buy-down of the rates. **SEN. HALLIGAN** said if 100% went to that, that helped us in the long run, but if you had the Universal Systems Benefits going into helping those programs, they retain the power bills, which would go back, then, to the same company. **SEN. HALLIGAN** asked **Mr. Richards** if he saw a problem with those two as opposed to going to the transmission, low interest loans or employee businesses. **Mr. Richards** replied the problem he saw with having the direct tax and the direct distribution back to in-state interests.

REP. FORRESTER said his contention all along had been that PSC said they had the authority to handle all of this. He asked **Susan Good** if this bill helped or hindered, or what this bill did as far as PSC stances in handling the whole matter. **Susan Good** responded as far as aiding or detracting from their own defense of assertion of their authority, the commission did not see a lot of impact with this bill. However, she added, they did have some serious concerns about the distribution, with them being the group to distribute the funds they would collect because, historically, they had never been part of anything like that. She said it was outside the goal of their mission.

REP. RONALD DEVLIN asked **Mark Richards** if there was a problem in the size of the generation unit as in Subsection 3. **Mr. Richards** said they did not see a problem with that.

REP. DEVLIN asked **Mark Richards** if there was no problem with exempting facilities under a certain size or over a certain size. He also asked, in **Mark Richards'** opinion, if there would be fewer legal ramifications in that way. **Mr. Richards** answered he had researched it thoroughly yet, but in his discussions with other attorneys in his office, they felt the state had a history of trying to help small business. He felt this would fall into that category.

REP. STORY asked **Mark Richards** about the first exemption of anything built after the date of the act. **Mr. Richards** answered they believed that exemption was also ok, under the theory that this would fit in the package of bills that would be coming through. He said the excess profits tax was designed to (1)try to curtail the high price of electricity and (2)to hopefully build on the market side also and give an incentive for the new generators. **Mr. Richards** added there was a rational basis for exempting new generation. He said if they were going to do it based on selling in the state of Montana, he would have a problem with it; but as written now, it was just a strict exemption for new generation and they believed that was ok.

REP. STORY asked **Mark Richards** if the second exemption was energy produced by a generation facility where at least 50% was used by that person. **Mr. Richards** replied they had talked about striking that portion in their discussions. He did not know if it was really that egregious, but he felt the object was to try to capture as much electricity generated in the state as possible.

REP. STORY asked **Mark Richards** about the qualifying facilities. **Mr. Richards** answered they had thought about striking that one also. He thought that one was based more upon trying to clean up the exemptions.

REP. STORY asked **Mark Richards** asked if they had to do #6, the federal facility. **Mr. Richards** answered yes.

REP. STORY asked **Mark Richards** about the 7th exemption dealing with the co-ops. **Mr. Richards** responded they had also discussed the co-ops and thought the coops were exempt in many places of the code. He believed that was in the spirit of the code.

SEN. COLE asked if the amendment going from 60-30 came from the house. Someone (cannot distinguish on tape who it was) replied yes.

SEN. COLE asked what the rationale was for the amendment. No one knew the rationale.

SEN. HALLIGAN asked **Mark Richards** what the average level of hydro-capacity was on the Missouri River for the dams. He asked if it was below 60. (Answer indiscernible on tape) **SEN. HALLIGAN** stated that exempted some PPL people on the dams as well.

SEN. HALLIGAN asked what if the default supplier was the person that held the account instead of the Public Service Commission. **Mark Richards** said he had not thought of that, so he didn't have an answer. **Jeff Martin** added he did not think state money could be directed to a private group indirectly. **Mark Richards** said it would be a distribution problem.

Jeff Martin said the Revenue Oversight Committee and the Revenue and Taxation Committee had looked at exemptions through the beneficial use tax. One of their concerns raised dealt with stacking exemption upon exemption. He said they may run into problems with the legality of applying for beneficial use tax such as on the power lines to just those specific entities. He recommended the committee keep that in mind when considering that area.

REP. DEVLIN told **Gene Walborn** he had commented earlier about how it would work with the Department of Revenue coming up with a form, come up with some sales and prices like that. **REP. DEVLIN** said it appeared that worked quite well if was an annual or multi-year contract. He wasn't sure how it work if there was excess power available for market. He asked how that would be recorded. **Gene Walborn** answered that might be in the form of a monthly return. He added the sport market gets excess electricity or energy to sell. **Mr. Walborn** said the department would need to see the contract, if there was one, and they would need to record that for each sale that was made because each sale could fall into a different tax structure. He said there might be a general form to list the amount and the provide all the detail for all the sales that fall into that particular tax rate. **Mr. Walborn** stated it could become very voluminous for all the spot market sales, however, it may be necessary to guarantee compliance.

REP. DEVLIN asked **Gene Walborn** if he was referring to each individual sale instead of a monthly average of a company's sales. **Mr. Walborn** responded that was the way he understood it. He said the company might submit the total amount in the monthly return. However, if the Department of Revenue wanted to verify that amount, the company would be required to provide documentation.

REP. FORRESTER asked **Will Rosequist** since the PSC had not regulated PPL for a number of years, was he sure \$45 was an

appropriate figure. He asked if that was something we would just guess at and place into law, then have PPL come forward and say \$45 was not an accurate figure. **REP. FORRESTER** stated the Department of Revenue said anything sold over \$45, if this bill passed, would be subject to tax. He again asked if **Mr. Rosequist** was sure the \$45 was appropriate. **Mr. Rosequist** responded he could not guarantee 100% that the \$45 was reasonable. He stated the commission, under a provision in federal law, would be given the ability to look at the books and records of a wholesale generator, such as PPL, to verify, if necessary, the \$45 was a reasonable figure to put into law. **Mr. Rosequist** said by having knowledge of what it cost NPC to generate with those assets during the period of time in which they did regulate them, and knowing what they sold for, it would be possible to compute with a fair degree of accuracy, what it cost PPL to generate with those same assets. He said the department had not undertaken that yet.

REP. FORRESTER asked **Will Rosequist** if he could give those figures to the committee with a high degree of accuracy within less than a week. **Mr. Rosequist** replied they could probably not get it done in a week, but they could try to accomplish that. He said they did have old information on what it cost MPC to operate those plants. He said he believed others may have already attempted to do the analysis, namely others involved in rate cases previously.

REP. FORRESTER asked **Will Rosequist** who would have that information then. **Mr. Rosequist** said he believed the Large Customer Group may have undertaken some sort of analysis.

REP. FORRESTER asked **Don Quander, Large Customer Group**, to comment. **Mr. Quander** responded they had done the analysis based on the cases they participated in because they created good analysis of what MPC's costs were and what the price paid by PPL was. He said they analyzed a range of costs to assure what kind of numbers would be precisely correct. He added the real answer was that the only party who could provide, with certainty in the next seven days, was PPL, and they had declined requests for the information. **Mr. Quander** told the committee PPL had declined to provide the cost information, even on a confidential basis, to the commission at this point. He said the analysis they had done showed anything under \$30 would generate a cost plus return, including pay-off of the debt. **Mr. Quander** said, in addition to their own analysis based on MPC's initial costs, they looked at two other things: (1) They looked at the fact that the contract PPL executed with MPC had ranged from slightly over \$18 to \$22.25. He said that was deemed an appropriate cost by both parties at that time. **Mr. Quander** said he presumed PPL would not

enter into contracts where they would think they'd lose money. He said the \$22.25 was the current regulated price. (2) He said the other indication they had was when PPL testified before the legislature requested property tax reduction. He said they indicated, at that time, they needed between \$28 and \$30 as a price on their power to cover their debt service in order to make as reasonable amount of profit as they expected in other buys.

Mr. Quander told the committee their best guess, based on certain assumptions about depreciation values and the interest rates used, was at \$45, the above cost amount varied between a minimum of 50% margin to 150% margin. He said \$30 was more than adequate. **Mr. Quander** stated he believed the Consumer Council submitted data, but they would have to speak for themselves to suggest that they think it was far below that.

SEN. HALLIGAN asked **Don Quander** if the debt included the \$780 million debt. **Mr. Quander** answered, "precisely". He added by that he meant the amount necessary to service traditional debt and pay off the purchase of the facility plus a 50% - 150% return on top of the pay-off of the debt.

SEN. HALLIGAN asked **Don Quander** to comment on the need to clean up the exemption issues and also the distribution issue. **Mr. Quander** concurred with the general point that additional exemptions could potentially raise issues. He said each of the issues were identified for particular reasons. **Mr. Quander** told the committee item #5 was the only exemption they felt would pose a problem as was currently written. Item number five dealt with electrical energy generated in Montana by a fully integrated regulated public utility and sold to customers within the authorized service territory of the public utility. He added the act was presently careful not to discriminate.

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Mr. Quander stated the intent of this was to protect or exempt sales by people that owned parts of Coal Strip that were regulated jurisdictions. He said the difficulty was there needed to be a rational basis for distinguishing between taxpayers in the consumer situation. He said the more appropriate rationale was for those selling pursuant to state commissioned and regulated tariffs and were historically an integrated utility, that may be a rational distinction between someone who was simply a wholesale generator selling in the wholesale market and somebody selling the bulk of their power pursuant to established regulated rates. He stated that was a meaningful distinction.

Mr. Quander told the committee they still had some concern about that exemption; they had concern about the way it was written as

well, preferring it would be written more narrowly instead. He said the owners were warranted.

SEN. HALLIGAN asked **Don Quander** if changing from the 60-30 megawatts would hurt or help. **Mr. Quander** replied it would help from a legal perspective. The bulk of the dams purchased by PPL were over 30 megawatts. By having a cut-off related to the size of the facility and new generation and other considerations would make this more legally defensible because there were other PPL dams below this size that were not subject to the tax sales.

REP. STORY asked **Dan Dodds**, according to EXHIBIT (1), if they sold for up to \$45, they would take home \$45; if they sold for \$60, would they take home \$57. **Dan Dodds** responded that was correct.

REP. STORY asked **Jeff Martin** if someone could look at the definition of "arms length transaction" and draft an amendment. **Jeff Martin** answered they would look into that request as it was of the more important aspects addressed in this bill.

ADJOURNMENT

Adjournment: 4:00 P.M.

SEN. MACK COLE, Chairman

LYNETTE BROWN, Secretary

BS/MC/LB

EXHIBIT (frs85sb0512aad)